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<Special Feature"Socio-Economic Role of Islamic Finance and its Potential in the Post-Capitalist Era">Resuscitation of the Antique Economic System or Novel Sustainable System? Revitalization of the Traditional Islamic Economic Institutions (Waqf and Zakat) in the Postmodern Era

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Resuscitation of the Antique Economic System or Novel Sustainable System? Revitalization of the Traditional Islamic Economic Institutions (Waqf and Zakat) in the Postmodern Era

NAGAOKA Shinsuke*

Abstract

The rapid growth of Islamic finance after 2000 has led to a new question on its practice. Critics of the current situation of Islamic finance contend that the newly developed Islamic financial products are not compatible with the ideal of Islamic economics, because these products are approved at patchwork screenings by a Sharia advisory board. After the middle of the first decade of the twenty first century, in order to overcome this situation, several new ideas were proposed by those who aspire the ideal of Islamic economics. First, they try to exploit the new areas of the practice of Islamic finance, where conventional finance could not ensure enough service or could cause negative effects. They focuses on microfinance lending and socially responsible investment (SRI) as concrete areas for applying Islamic finance. Second they recently focuses on the traditional Islamic economic institutions like *waqf* and *zakat*. The practices of these institutions are still alive in the contemporary Islamic world, although they are getting scarce in many regions. They are trying to activate these institutions using the scheme of Islamic finance, tapping a new market for Islamic finance. This paper identifies these new trends in Islamic finance, and considers the characteristics of the trends and historical implications, in particular, examines whether this revitalization can be regarded as the resuscitation of the antique Islamic economic system or the emergence of a novel system.

I. Introduction

After its boom in the 2000s, the practice of Islamic finance faces criticism by those who aspire the ideal of Islamic economics. They contend that the newly developed Islamic financial products are not compatible with the ideal of Islamic economics, because these products are approved at patchwork screenings by an internal Sharia advisory board. At the next section, this paper firstly clarifies the theoretical framework and historical background of the criticism by picking up two prominent previous instances which were found in the history of Islamic finance since 1970s.

After the middle of the first decade of the twenty first century, in order to overcome this situation, several new ideas were proposed by both bankers and scholars. These ideas

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can be divided into two trends; 1) development of the new areas of the practice of Islamic finance, where conventional finance could not ensure enough service or could cause negative effects, 2) revitalization of the traditional Islamic economic institutions like *waqf* and *zakat* by utilizing the scheme of Islamic finance. At the subsequent section, this paper identifies these new trends in Islamic finance, and attempts to clarify the theoretical and practical issues. As for the second trend, the paper especially clarify the following issues with concrete case studies. 1) How does the scheme for revitalizing these traditional institutions work in practice? 2) How does the contemporary Islamic jurisprudence innovate the interpretations in order to implement the scheme of Islamic finance into the *waqf* and *zakat*?

Finally based on these analyses, this paper analyzes the characteristics of the trends, and considers the historical implications of revitalization of these traditional institutions and, in particular, examines whether this revitalization can be regarded as the resuscitation of the antique Islamic economic system or the emergence of a novel sustainable system, which can provide an alternative to the current capitalistic system.

II. Islamic Finance and the Criticism of its Practice

2.1. Theoretical Framework of the Criticism

Since the rise of its commercial practice in the 1970s, Islamic finance has confronted inherent problems related to its practical survival that are not observed in conventional finance. As unanimously agreed by the bankers and the researchers in this field, all the services of Islamic finance must be compliant with the teachings of Islam; the existing Islamic financial institutions certainly attach high importance to this condition, which this paper calls “Sharia Legitimacy Condition (SLC).” In order to be commercially successful in a situation where its practice coexists with conventional finance, Islamic finance needs to provide competitive financial products that are acceptable by all customers (both Muslims and non-Muslims); this condition is called the “Economic Feasibility Condition (EFC)” by this paper. Thus, the practice of Islamic finance must maintain a balance between the above two conditions in order to survive as a financial practice.

However, most practices of Islamic finance do not necessarily satisfy both the conditions. Many controversies regarding this matter, for example, determining which condition must or should be considered more important by Islamic finance, have been observed throughout the history of this field. In order to understand tension between the two conditions (SLC and EFC) with concrete examples, the following section overviews the most prominent cases at the early and middle stages of Islamic finance: the *murabaha* issue in the 1980s, the *bay ina & bay dayn* issue in the 1990s.

2.2. Conflict and Coordination between the Two Conditions (SLC and EFC)

2.2.1. *Murabaha* Issue in the 1980s

Before the rise of the commercial practice, there appeared to be a consensus in Islamic economics regarding preferable financial products for Islamic finance operations. Most Islamic economists (for example, Mahmud Ahmad, Muhammad Uzair and Muhammad Nejatullah Siddiqi) encouraged profit-sharing-based financial products such as *mudaraba* and *musharaka*.¹ The author calls this consensus the “*Mudaraba* Consensus” (Nagaoka, 2012: 118). However, from the 1970s onward, the practice of Islamic finance did not necessarily reflect the theoretical suggestions made by Islamic economists prior to that period. Most Islamic banks mainly adopted *murabaha* on their asset side as an alternative financial product for interest-based loans in conventional finance. With regard to the share of *murabaha*, the majority of Islamic banks in both the Gulf countries and Malaysia have shown a widespread preference for *murabaha*.² Such a preference can be observed almost throughout the period beginning from the 1980s until now. According to al-Harran’s aggregate calculation, it is estimated that 80-90% of financial products instruments on the asset side of Islamic banks were based on *murabaha* from the 1970s through the first half of the 1990s, which implies that the share of profit-sharing-based instruments was meager (al-Harran, 1995: xi).

In response to this situation, many criticisms and arguments against *murabaha* were advanced in the 1980s not only because profit-sharing-based financial instruments were rarely used on the asset side of Islamic banks but also because *murabaha* involved certain contentious issues from the viewpoint of Islamic jurisprudence. Many Islamic economists, who emphasized their ideal of the Islamic economic system where a profit-sharing-based system achieves desirable economic performance from the aspect of Islam (therefore, they attached importance to Sharia Legitimacy Condition, SLC), were skeptical about the legitimacy of *murabaha* from the viewpoint of its similarity to transactions such as interest-based loans where *riba* (almost equal to “interest” in a modern sense) is charged.³ On the other hand, Islamic economists who emphasized the economic feasibility of Islamic finance practice (therefore, they attached importance to Economic Feasibility Condition, EFC), promoted *murabaha* with approvals by Sharia scholars who belong to the Sharia supervisory board in Islamic banks. Many supportive Sharia scholars acquired the legitimacy of *murabaha* by explaining that unlike the profits (interest receipts) in conventional loans any profits should be expressed as a function of supply and demand in the real goods market, not in the monetary market.⁴

1 For more details, see their books (Ahmad, M., 1947; Uzair, 1978; Siddiqi, 1983(1969)).

2 For the concrete statistics calculated by the author, see (Nagaoka, 2012: 122–123).

3 For example, see Ziauddin Ahmad’s argument (Ahmad, Z., 1985: 19–20).

4 For example, see the *fatwa* issued at the 1st Albaraka Symposium held in 1983 (English translation

2.2.2. *Bay Ina & Bay Dayn* Issue in the 1990s

Generally in banking operations, there is a liquidity gap between the liability side and asset side of banks. Therefore, all the banks need to manage their liquidity in the interbank market. However, Islamic banks cannot work in such a market because the products there involve the element of *riba*. In the 1980s, there were limited opportunities for Islamic banks to manage liquidity owing to the lack of useful tools. As for the experience of Islamic banks in both the Gulf countries and Malaysia, most Islamic banks must maintain substantial liquidity in order to be prepared for a potential liquidity crisis. In the 1990s, Malaysia became proactive about the liquidity issue and led innovation in liquidity management tools (LMTs) in Islamic finance. In 1993, it established the Islamic Interbank Monetary Market (IIMM) and introduced various LMTs for Islamic banks. Although *mudaraba* Interbank Investments (MII) attracted interest among the LMTs, they faced the same inherent problem as an original *mudaraba* and failed to gain popularity. As a result, most Islamic banks and Islamic windows in Malaysia began using other LMTs, particularly *bay ina & bay dayn* based tools. *Bay ina & bay dayn* tools have two practical advantages over MII; the first is a high tradability that means it is “easy to sell the title of liquidity in the secondary market.” The other is that these tools enable Islamic banks to calculate their profit in advance.

However, like *murabaha* in the early stage of Islamic finance, *bay ina & bay dayn* based tools also faced controversy in the 1980s. Although these tools were approved by Malaysian Sharia scholars through several legal resolutions (Sharia Advisory Council at both Securities Commissions Malaysia and Bank Negara Malaysia),⁵ most Sharia scholars in the Gulf countries did not approve these tools from the aspect of legitimacy. With regard to *bay ina*, they criticized that its form is that of fictitious double trades targeted at raising funds, which is very similar to interest-based loans.⁶ As for *bay dayn*, they were skeptical about the sales of debts at a discounted price, which are similar to exchanges of money.⁷ In accordance with the objection by Sharia scholars, most Islamic Banks in the Gulf countries in the 1990s did not adopt *bay ina & bay dayn* based LMTs, and continued to face a liquidity management problem.

Interestingly, the case in the 1990s shows that the controversy emerged as “regional” theoretical differences. While Sharia scholars, Islamic economists and bankers in the Gulf countries put a high priority on Sharia Legitimacy Condition (SLC), those who are in Malaysia put a high priority on Economic Feasibility Condition (EFC). Based on this regional

available at (Nagaoka, 2007: 75–76)).

5 For example, see the resolutions issued at the 2nd & 5th meetings of the Sharia Advisory Council at Securities Commissions Malaysia in 1996 & 1997, and the 8th meeting of the Sharia Advisory Council of at Bank Negara Malaysia in 1998.

6 For example, Taqi Usmani’s opinion (Usmani, 2001: 113).

7 For example, see the *Fatwa* issued at the 11th meeting of the OIC *Fiqh* Academy (*Majma’ al-Fiqh al-Islami al-Duwali*) in 1998.

theoretical differences, the practice of Islamic finance in the 1990s diverged in two directions; the Gulf and Malaysian practices.

2.3. Rapid Growth of Islamic Finance and the Criticism to “Sharia-Compliant Finance”

The commercial practice of Islamic finance rapidly grew after 2000 in terms of both numbers and spread. The average annual growth rate after 2000 was over 20%, and the total assets of the Islamic financial industry reached 1.4 trillion USD at the end of 2012 (TheCityUK, 2013). Although the market share of Islamic finance in the world is under 1%, its share in developing and emerging countries is 15%.⁸ Therefore, the practice of Islamic finance is expected to expand worldwide in the near future if we consider its potential economic growth.

One of the key factors in the rapid growth of Islamic finance is the development of new financial products, some of which have been mentioned above: *sukuk*, commodity *murabaha*, and Islamic derivatives. These products were developed to match the development of conventional finance and maintain competitiveness. Since their development, Islamic finance has succeeded in taking a certain portion of market share.

However, the situation of Islamic finance in the 2000s stimulated the tension between the two conditions (SLC and EFC) because the new products mentioned above were developed giving high priority to marketability. Generally speaking, each Islamic bank has its own Sharia Supervisory Board consisting of prominent Muslim jurists that judges the compatibility of the products with the teachings of Islam. Of course, these controversial products are also approved by the board. However, criticisms have been raised against the focus of Muslim jurists on the Sharia compliance of each product, on an individual basis, and not considering the compatibility of Islamic financial products as a whole and their purpose. Mahmoud El-Gamal who radically criticizes the current situation of Islamic finance calls such a process of approving products “Sharia Arbitrage” (El-Gamal, 2006: 174), and the critics generally use the term “Sharia-compliant finance” to criticize the current situation of commercial Islamic finance.⁹

III. New Horizon’s in Islamic Finance

After the middle of the first decade of the twenty first century, new trends that put a high priority on Sharia Legitimacy Condition (SLC) emerged in Islamic economics in order to overcome the current situation faced by Sharia-compliant finance. This paper defines two such trends: the first trend, called “New Horizon 1.0,” pertains to the development of new areas in the practice of Islamic finance; the second trend, called “New Horizon 2.0,” pertains to the

⁸ Except China and India. Calculated by the author based on (McKinsey Global Institute, 2009; TheCityUK, 2013)

⁹ The most controversial case of Sharia-compliant finance is *tawarruq*. For more details on the case, see (Nagaoka, 2012: 127–129).

revitalization of the traditional Islamic economic institutions by utilizing Islamic finance.

3.1. New Horizon 1.0: Development of New Areas in Islamic Finance

The incubators of this trend attempt to exploit new areas in the practice of Islamic finance, where conventional finance cannot ensure enough service or may create negative effects (Asutay, 2007: 16). In order to provide representative examples, this paper focuses on microfinance lending and socially responsible investment (SRI) as concrete areas for the application of Islamic finance.

3.1.1 Islamic Microfinance

Since the resounding success of Grameen Bank during the 1980s, many microfinance institutions have been established across the world. Therefore, the idea of microfinance does not originate from Islamic finance. However, the scheme of microfinance shares common aspects with *mudaraba* and *musharaka*, in terms of the mechanism that makes a lender responsible for the business of a borrower. It is worth noting that the pioneering Islamic banker Ahmad al-Najjar, who established the Mit Savings Ghamr Bank in Egypt in 1963, had proposed an idea similar to microfinance (al-Najjar, 1972).

Islamic microfinance is practiced very actively in several Muslim countries such as Indonesia and Iran. In the case of Indonesia, although the authorities concerned have not established a formal category for “microfinance institutions,” “Bank Perkreditan Rakyat” (BPR, rural banks), under the supervision of the Bank Indonesia (Central Bank of Indonesia), and “financial cooperatives,” under the supervision of the Ministry of Cooperatives and Small-Medium Enterprises, can be considered as microfinance institutions owing to the nature of their services. Amongst these institutions, BPR Syariah (BPRS) and BMT (Baitul Maal wat Tamwil, Islamic cooperatives) provide Islamic financial services. Both BPRS and BMT were first established in the early 1990s (Seibel, 2012: 149–151) and have grown rapidly ever since. Currently there are 158 BPRS¹⁰ and over 3,500 BMT¹¹ branches in Indonesia. Although the percentage share of each institution (BPRS in all BPRs, BMT in all financial cooperatives), in terms of number of branches, is still small (BPRS: 4%, BMT: 7.2%) (Seibel, 2012: 150–151), the potential of BPRS and BMT in the Indonesian economy and society seems significant in relation to the world’s largest Muslim population in Indonesia as well as the current government policy for promoting Islamic finance (Ismal, 2013: 15–28).

Askari et al. (2009) and Hitoshi Suzuki (2010) demonstrate the experience of Islamic microfinance in Iran. According to their works, many Islamic microfinance institutions under the name of Gharzul-Hasaneh Funds (GHFs) have been in existence since

¹⁰ Data based on the author’s independent field survey in March 2013.

¹¹ Data based on (Hamada, 2010: 222).

1969,¹² implying that GHFs were functional long before the Iranian Islamic Revolution of 1979 (Askari et al., 2009: 202; Suzuki, 2010: 132). After the revolution, the number of GHFs started to increase owing to the religious motives and complementary functions of nationalized commercial banks. Although the deposit share of GHFs decreased during the late 1980s and early 1990s, the situation subsequently improved and the number of GHFs started to increase again in the late 1990s. One of the reasons was that GHFs fulfilled the financial demand of the emerging small and medium enterprises in rural areas during President Hatami's reforms (Suzuki, 2011: 133). Although the operations of GHFs are highly dependent on the political situation, as mentioned by Suzuki (2011: 136), currently GHFs not only have an established role in the financial sector of Iran, but also provide a role model for the newly-branded Islamic commercial banks in Iran.¹³

Based on its recent growth, Islamic microfinance has started to attract increasing attention of both academic researchers and practitioners. Recently, several benchmark works in Islamic economics have been published.¹⁴ Along with widespread recognition, we can find some recent examples of countries, such as sub-Saharan African countries, where the practice of Islamic microfinance preceded the commercial practice of Islamic finance.¹⁵

3.1.2 Islamic SRI

The proposal for Islamic SRI is in line with the global trend in SRI, that is, corporate stakeholders assign a higher priority on companies that are engaged in social welfare activities. However, unlike conventional SRI, Islamic SRI includes religious aspects of corporate activities and social action programs, such as educational, welfare, and medical services, through the payment of *zakat*. Most Islamic banks are very positive in contributing towards these sectors.

In addition, the exclusion of incompatible businesses in the light of Islamic teachings is also a distinctive feature; for example, gambling (casinos, horse racing), unethical businesses (military, pornography industry), and un-Islamic transactions (deals involving alcohol and pork, issuing interest-bearing corporate bonds) are forbidden.

Recently, Sharia indices for the stock market have been developed in order to identify companies that keep their businesses compliant with Islamic teachings. Here, rating agencies such as FTSE and S&P screen corporate activities and disclose the results of screening in the form of Sharia indices. For example, FTSE began releasing the FTSE Global Islamic Index

¹² *Gharzul-hasaneh* is Persian literature; *qard hasan* in Arabic.

¹³ Bank Mehr Iran, known as the first newly-branded Islamic bank in Iran, mainly provides services based on the scheme of *gharzul-hasaneh*.

¹⁴ For example, (al-Harran et al., 2008; IRTI, 2008; Obaidullah, 2008; Ali, 2012).

¹⁵ Islamic Saving and Credit Cooperative of Cameroon was established in Cameroon in 2008. In 2010, Ghana Islamic Microfinance was established in Ghana, and Al-Barakah Microfinance Bank in Nigeria.

in 1998; Dow Jones and the Kuala Lumpur Stock Exchange (now Bursa Malaysia) began releasing their own Sharia indices in 1999. These indices select companies that are compliant with Islamic teachings based on their own respective criteria (see Table 1).

FTSE and Dow Jones provide more detailed indices that are customized for each region, including not only Islamic but also non-Islamic countries. As in the case of Japan, a representative non-Islamic country, both FTSE and S&P have disclosed indices targeting Japanese companies as “FTSE Shariah Japan 100 Index” (since 30 July, 2007) and “S&P/TOPIX 150 Shariah Index” (since 3 December, 2007), respectively. Therefore, Japanese companies have already screened from the viewpoint of Islamic finance.

Table 1: Difference of Criterion in Sharia Indices

	Sharia Criteria of Core Activities	Financial Ratio Filtering
Dow Jones Islamic Index	alcohol, tobacco, pork-related products, conventional financial services (banking, insurance, etc), weapons and defense, entertainment (hotels, casino/gambling, cinemas, pornography, music etc)	less than 33%: total debt divided by trailing 12-month average market capitalization, the sum of company's cash and interest bearing securities divided by trailing 12-month average market capitalization, account receivables divided by trailing 12-month average market capitalization
FTSE Islamic Index	conventional finance (non Islamic banking, finance and insurance, etc), alcohol, pork-related products, entertainment (casinos/gambling, pornography, cinemas, music, hotel, etc), tobacco, weapons and defense	less than 5%: non-compliant income other than interest, total interest income less than 33%: debt divided by total assets, cash and interest bearing items less than 50%: account receivables and cash purification ratio: 5% of dividends
Bursa Malaysia	financial services based on <i>riba</i> , gambling, manufacture or sale of non- <i>halal</i> products, conventional insurance, entertainment activities that are non-permissible according to Sharia, manufacture or sale of tobacco-based products or related products, stock-broking or share trading in Sharia non-approved securities, other activities deemed non-permissible according to Sharia	5% criteria: clearly prohibited activities (<i>riba</i> , gambling, selling pork or liquor) 15% criteria: prohibited element affecting most people and difficult to avoid (<i>umum balwa</i>) 20% criteria: mixed rentals, rental from premises used in gambling, sale of liquor, etc 25% criteria: generally permissible and would bring benefits, hotel and resort operations, stock-broking, share trading

Source: (SC, 2009: 20-21) with the author's revision.

3.2. New Horizon 2.0: Revitalization of the Traditional Islamic Economic Institutions

In addition to the trend of “New Horizon 1.0” (development of new areas in the practice of Islamic finance, as discussed previously), recently a fresh trend (called “New Horizon 2.0” in this paper) has emerged which attempts to revitalize the traditional Islamic economic institutions, such as *waqf* and *zakat*, using the scheme of Islamic finance. Although the practices of these institutions are still functional in the contemporary Islamic world, their respective roles in each national economic system are decreasing. This attempt at revitalizing these institutions aims to re-evaluate their roles for the sustainable development of the Muslim community, as well as for tapping new markets for Islamic finance. Through providing representative examples, this paper focuses on both *waqf* and *zakat* as concrete areas for the application and utilization of Islamic finance.

3.2.1. *Waqf*

Waqf is a property donated by the owner (*waqif*). The administrator (*nazir*) is entrusted by the *waqif* to manage the property and to distribute the revenues to specific or charitable purposes. *Waqf* was prevalent throughout the majority of the Islamic world in the pre-modern era, and played an important role in the Islamic economy and society. After the advent of the modern era, the practice of *waqf* has been declining in many regions owing to colonization and westernization. Some of the Middle Eastern countries abolished the family *waqf* (*waqf ahli*) during the middle of the twentieth century,¹⁶ and many Islamic countries nationalized the charity *waqf* (*waqf khayri*), resulting in inefficient administration (Rashid, 2003: 9–14).

Recently, several countries have attempted to revitalize *waqf* properties in order to generate additional revenues for the socio-economic betterment with sustainable development of the Muslim community. The typical way of revitalizing is through rebuilding and renovation of *waqf* properties. Here, two issues arise in the rebuilding and renovation of *waqf* properties; the first issue is a legitimacy problem, that is, how such rebuilding and renovation activities can be legitimized from the Islamic viewpoint; while the second issue is a funding problem, that is, how to raise funds for such rebuilding and renovation activities. Regarding these issues, this paper selects the case of Singapore as an innovative example.

Singapore is one of the pioneering countries in the revitalization of *waqf* properties, in terms of both practice and development of institutional infrastructure. In Singapore, the Islamic Religious Council (Majlis Ugama Islam Singapura, MUIS) mainly undertakes the revitalization of *waqf* properties in the country, while the *fatwa* committee at MUIS develops a theoretical framework for it.¹⁷

¹⁶ The year of abolishment in each country is as follows: Turkey, 1926; Syria, 1949; Egypt, 1952; Tunisia, 1962-63; Libya, 1973; United Arab Emirates, 1980 (Rashid, 2003: 9).

¹⁷ The following analysis of Singapore mainly refers (Abdul Karim, 2010) as an information source.

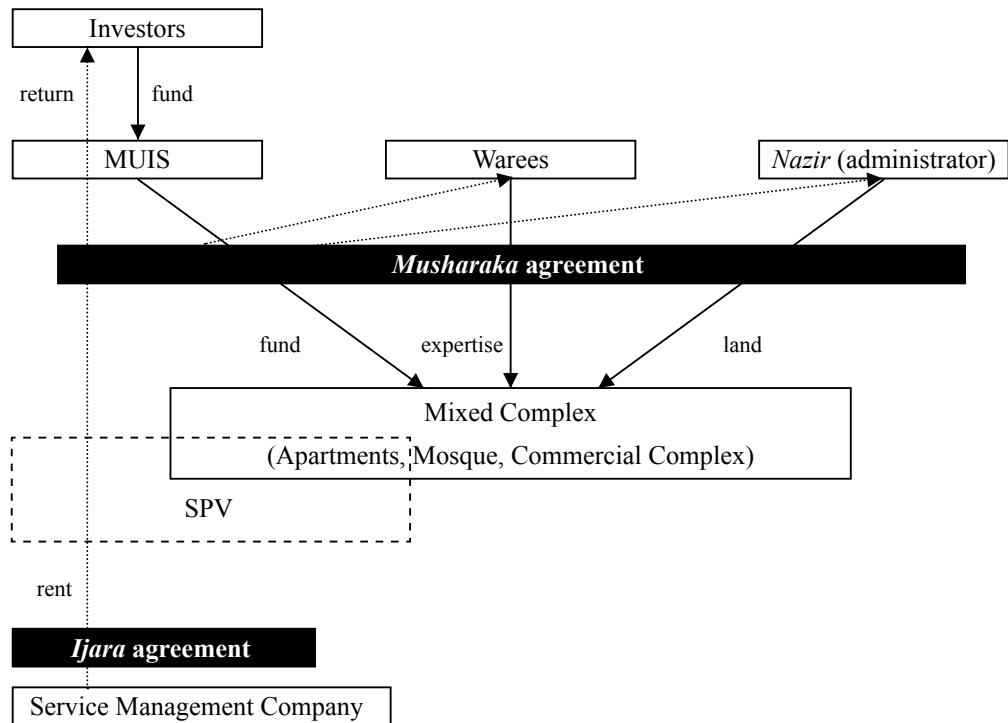
Regarding the first issue (legitimacy problem) as mentioned above, the *fatwa* committee uses the concept of *istibdal* for the rebuilding and renovation of properties. The term *istibdal* stems from *ibdal*, which means to take out a consecrated substance from the original stipulation of the *waqf* in exchange for another substance which makes the latter a *waqf* in place of the former (Mahamood, 2006: 49). MUIS uses this basic idea of *istibdal* for rebuilding, renovation, and relocation of the *waqf* properties under the following four conditions stipulated by the *fatwa* committee: 1) the assets are in a dilapidated state, 2) the assets are in danger of acquisition, 3) the assets are located in an unsuitable location such as a promiscuous area, and 4) the assets can yield better returns through relocation and redevelopment (Abdul Karim, 2010: 148).

As for the second issue (funding problem), MUIS raises funds for rebuilding and renovation through several ways; internal funding through Baitulmal fund;¹⁸ long lease (*hukr*),¹⁹ sale of existing properties, and external financing (Abdul Karim, 2010: 149–154). A third way of raising funds is that Islamic finance can engage in the revitalization of *waqf* properties. Shamsiah Bte Abdul Karim shows the prototype case of raising funds through *sukuk* scheme (see Figure 1) (Abdul Karim, 2010: 152–154). First, MUIS, Warees (a subsidiary of MUIS to handle *waqf* properties), and the *nazir* (administrator of the *waqf*) enter into a joint venture agreement (*musharaka*) to construct a mixed-use complex comprising a mosque, commercial complex and apartments. While MUIS provides funds collected from investors who receive certificates (*sukuk*), Warees provides its professional expertise, and the *nazir* contributes land and some capital. After completion of construction, the special purpose vehicle (SPV) of this joint venture enters into an *ijara* (leasing) contract for the apartments with a service management company. Here, the rent of the apartments is paid to the SPV, which is then subsequently distributed amongst the three parties of the *musharaka* agreement in accordance with their respective contributions.

In addition to utilizing Islamic finance for raising funds to revitalize *waqf* properties, a new idea of creating a linkage between *waqf* and Islamic finance is currently being proposed, namely, that Islamic finance utilize the funds of cash *waqf* (*waqf nuqud*) through its schemes (*mudaraba*, *musharaka*) and generate revenues for the socio-economic development of the Muslim community (Lahsasna, 2010; Çizakça, 2011). Although this idea has not yet been implemented, it implies a great potential for collaboration between *waqf* and Islamic finance in the contemporary world.

18 Baitulmal fund is the institution that acts as a trustee for the Muslims. MUIS allocates the funds for public and community projects and general welfare. The source of the funds is primarily from the estate of a deceased person (<http://www.muis.gov.sg/>).

19 The concept of *hukr* grants the tenant of the *waqf* property a priority of lease, the right of permanent lease, or the perpetual right to the usufruct of the *waqf*. The occupant either pays a variable rent during the lease period that changes as the value of the property changes, or a fixed rent (Dallal, 2004: 26–27).

Figure 1: Fund Raising for *Waqf* Properties through *Sukuk* Scheme

Source: Author's own based on information at (Abdul Karim, 2010).

3.2.2. Zakat

Zakat payment, as one of the most important obligatory deeds, has been performed by every eligible Muslim all across the Islamic world. However, the role of *zakat* is not necessarily significant in terms of a national economy in aggregate in the modern age. This is because, with the exception of a few countries, there are no official entities responsible to comprehensively collect and disburse *zakat* payments; the management of *zakat* (collection and disbursement) in most Islamic countries is segmentalized and is performed by the respective local Muslim communities. Since the rise of Islamic finance in the 1970s, Islamic banks and financial institutions have been very positive in opening specific accounts for *zakat* payments. They collect *zakat* funds not only from their own revenues, but also from customers' dividends earned on *mudaraba* deposit accounts under the agreement. This implies that the role of *zakat* can be significant in terms of a national economy in accordance with the growth and expansion of Islamic finance in the country.

Recently, the United Arab Emirates (UAE) commenced innovative attempts at collaboration between *zakat* and Islamic finance.²⁰ There is a sovereign entity called the

²⁰ The following analysis of the UAE is mainly based on the author's own field research conducted in

“Zakat Fund” (ZF, *Sundug al-Zakat*) for collecting and disbursing *zakat* in the UAE. In 2010, Abu Dhabi Islamic Bank launched a new service to collect *zakat* on behalf of ZF through the bank’s ATMs, mobile phones and the bank counters at its branches. In addition, ZF installed its own ATM machines for collecting *zakat* in 2011. Using these ATMs, customers can not only pay *zakat* but can also indicate the category of disbursement of *zakat*. It seems that these attempts would make the management of *zakat* more efficient and comprehensive.

According to the author’s own field research, ZF has several plans in place for further development of the management of *zakat*. First, ZF plans to add a function for receiving *zakat* money using ATMs. Here, ZF annually screens the *zakat* recipients and grants these recipients a card. The recipients insert the card into the ATMs to receive *zakat* at any time they wish. Second, ZF also plans to utilize *zakat* funds for financing development projects and trade ventures in order to expand its disbursement base. Regarding this matter, there is controversy on the legitimacy of turning over *zakat* funds. According to a brief survey conducted by Shah Haneef and Mahmud (2011: 75–77), those who contest the utilization of *zakat* funds insist that *zakat* is not supposed to be reserved for future needs, rather it is primarily designed to alleviate the present economic needs of the recipients; therefore, the collected *zakat* should be promptly distributed to its recipients. On the other hand, those who support the utilization of *zakat* funds state that the disbursement of *zakat* does not have to be prompt; therefore, investing *zakat* funds is permissible if the following three conditions are satisfied; 1) the ultimate ownership of its return and the capital sum be spent on the recipients, 2) only surplus funds should be invested, and 3) investment activities should be carried out using extra caution and prudent financial planning so as to avoid losses to the pool of *zakat* property. Although it would take much longer to settle the controversy, the innovative attempts by ZF would serve as a test in paving the way for a substantive linkage between *zakat* and Islamic finance.

IV. Resuscitation of the Antique Economic System or Novel Sustainable System?

Finally, this paper analyzes the characteristics of these new trends (“New Horizons 1.0 and 2.0”) in Islamic finance, and then considers the historical implications.

Before the emergence of new trends, Islamic finance was functioning as an autonomous financial sector, although it had been contributing towards the development of the economy and society as an intermediary for monetary flows. After the emergence of new trends, Islamic finance has become deeply ingrained in both the economy and society by broadening the range and types of services. For example, Islamic microfinance enables pious but poor people to have easy access to retail financial products while maintaining their beliefs, which leads to an improvement in their standard of living. The concept of Islamic SRI has enabled us to

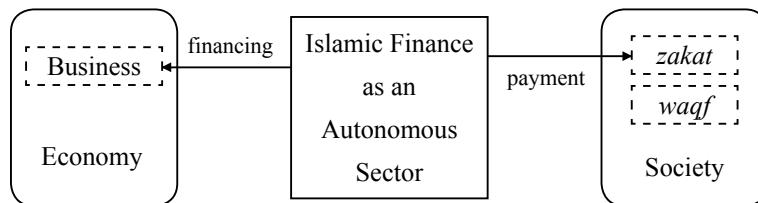
September, 2011.

recently recognize the importance of Sharia legitimacy for the contents of business enterprises as Islamic investment destinations, besides the legitimacy of financial services. The popularity of Islamic SRI is one of the important factors in explaining the recent rise of the so-called Islamic businesses, such as *halal* products (food, cosmetics), Islamic clothing for Muslim women, and Islamic tourism. As for *waqf* and *zakat*, Islamic finance provides important ideas for revitalizing these traditional institutions, and contributes to the socio-economic development of the Muslim community.

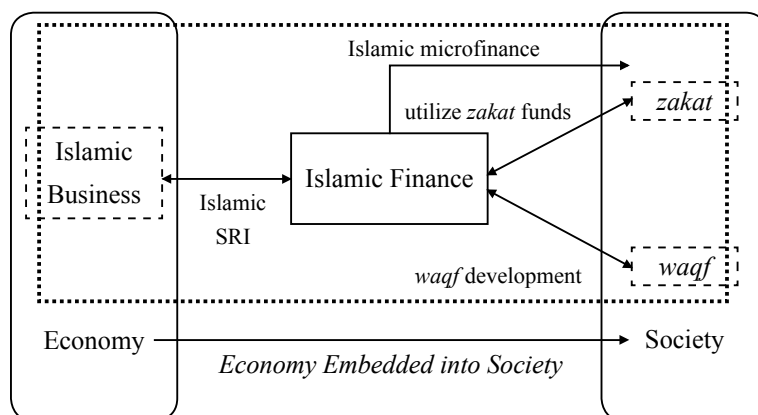
It can be said that the involvement of Islamic finance in the economy and society in various ways implies that the new trends in Islamic finance are conducive to the organic integration of the Islamic economic system in the modern world. In this system, profits from businesses can be efficiently redistributed to society through Islamic finance; therefore, Islamic finance plays an important role in the system as a medium to embed the economy into society, implying a counter-vision of the current capitalist system (see Figure 2).

Figure 2: Organic Integration of the Islamic Economic System in the Modern World

(a) Before Emerging the New Trends



(b) After Emerging the New Trends

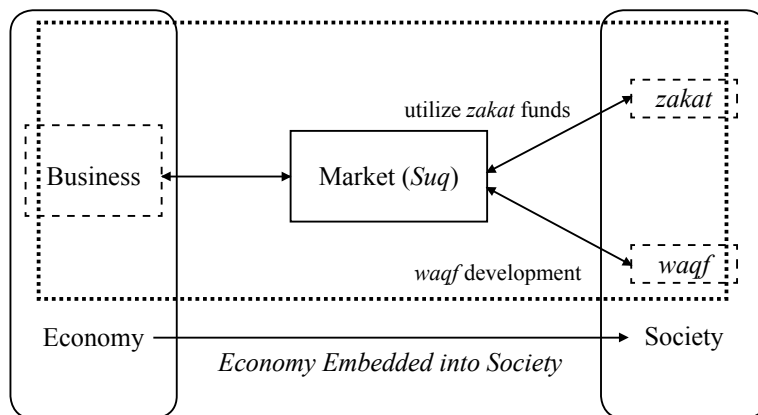


Source: Author's own.

Based on the clarification of the characteristics of the new trends in Islamic finance, this paper considers whether this Islamic economic system with organic integration in the modern

world can be perceived either as a resuscitation of the antique Islamic economic system in the pre-modern Islamic world, or as the emergence of a novel sustainable system. When we trace back to history, it can be observed that the Islamic world had such an integrated economic system in the pre-modern era. According to Hiroshi Kato's theoretical work on the economic system of the pre-modern Islamic world (Kato, 2002), the open market policies pursued by the Islamic dynasties and the prevalence of the economic institutions such as *waqf* and *zakat* constituted the highly integrated economic system. For example, large-scale *waqf* properties were usually established as a combination of commercial estates (markets, accommodation etc.) and charitable (hospitals, asylums etc.) or religious (mosques etc.) estates. When revenue was generated through commercial activities in the market, it was promptly distributed amongst charitable and religious purposes. There, a market (*suq* in Arabic) took a part of the medium of the system and integrated the economy with society (see Figure 3). It is easy to understand that the organic integrated model in the modern world can share its nature with the economic system in the pre-modern Islamic world.

Figure 3: Economic System in the Pre-modern Islamic World



Source: Author's own based on the theoretical work of (Kato, 2002).

Then, we should consider whether the Islamic economic system with organic integration in the modern world is just a resuscitation of the antique system. The novelty of the emerging system is based on modern technology, especially cyber networks. Through this network, we can conduct remote transactions, for example, between Malaysia and the Gulf countries round the clock daily. This characteristic implies that the emerging system forms a transnational network that exists not at the real geographical level but at a meta-geographical level.

V. Conclusion

This paper focused on new trends in Islamic finance after the Sharia compliant criticism in

the middle of the first decade of the twenty first century, and classified these into two trends. The first trend, which the paper calls “New Horizon 1.0,” pertains to the development of new areas in the practice of Islamic finance, and the paper discussed Islamic microfinance and Islamic SRI as examples. The second trend, which the paper calls “New Horizon 2.0,” pertains to the revitalization of the traditional Islamic economic institutions through utilizing the scheme of Islamic finance, and the paper discussed *waqf* and *zakat* as examples. The primary characteristic of these new trends is that Islamic finance is significantly involved with the economy and society in various ways. This implies that the new trends in Islamic finance are conducive to the organic integration of the Islamic economic system in the modern world. When we trace back to the history of the Islamic world, we observe that the nature of the emerging system shares commonality with that of the economic system in the pre-modern Islamic world, in terms of high integration with economy and society. However, this paper highlighted that the emerging system came into existence based on the modern cyber technology. This enabled the system to exist not at the real geographical level but at a meta-geographical level. Therefore, it can be concluded that the system is not just a resuscitation of the antique economic system in the pre-modern Islamic world, but is also a novel system that succeeds the golden heritage of the pre-modern era.

For further discussion, it is worth mentioning that the meta-geographical nature of the emerging system is quite important for considering the future vision of the economic system for humanity. This is because the spirit of the emerging system, which embeds the economy into society, raises sympathy amongst many people in many regions and becomes very easy for these people to introduce or join the system. This implies that not only there is a potential for the system to spread globally, but also a great potential to become an alternative choice for the next universal economic system with sustainable development.

In addition, as discussed in the paper, these new trends emerged as a result of the criticism on the current practice (called “Sharia compliant finance”) of Islamic finance. Some researchers and bankers argue for the need to standardize regulations and products in Islamic finance in order to reduce controversies. However, when we consider the source of the emergence of new trends, the controversy between Sharia Legitimacy Condition (SLC) and Economic Feasibility Condition (EFC), as reviewed in the paper, becomes very important for further innovative developments in Islamic finance; radically speaking, the controversy guarantees the future of Islamic finance. Therefore, it would be very important to ensure the arena for sound discussions amongst Sharia scholars, researchers, and bankers.

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